United States Court of Appeals

for the Second Circuit

APPELLANT'S REPLY BRIEF

76-7465

United States Court of Appeals

For the Second Circuit

TRANSCONTINENTAL OIL CORPORATION, TRECON OIL CO. LTD. and B. EDWIN SACKETT, individually and as nominee,

Plaintiffs-Appellees and Cross-Appellants,

—against—

TRENTON PRODUCTS COMPANY, BERNARD FEIN, HERZFELD & STERN, LOEB, RHOADES & CO., GERSTLEY, SUNSTEIN & COMPANY, A. ARTHUR WEISS, LOUIS C. FIELAND and THERESA ZAPPLEY,

Defendants.

TRENTON PRODUCTS COMPANY and BERNARD FEIN,

Defendants-Appellants and Cross-Appellees.

TRENTON PRODUCTS COMPANY and BERNARD FEIN,

Defendants and Third-Party Plaintiffs—Appellants and Cross-Appellees,

—against—

PHILLIP P. GOODKIN, LOUIS GOODKIN, MICHAEL A. ROBERTS, DAVID FRANKEL, JAMES E. DAVIS, PAUL A. ROSSBOROUGH, J. STREICHER & COMPANY, HARRY B. LESLIE, BERTRAM F. FAGENSON, EDWIN B. SACKETT and FAGENSON AND FRANKEL COMPANY, INCORPORATED,

Additional Defendants—Appellees on Counterclaim.

Appeal from a Judgment of the United States District Court for the Southern District of New York

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REPLY BRIEF OF DEFENDANTS-APPELLANTS TRENTON PRODUCTS COMPANY AND BERNARD FEIN

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Preliminary Statement

Defendants-Appellants and Cross-Appellees, Trenton Products Company ("Trenton") and Bernard Fein ("Fein")* jointly submit this reply brief in support of defendants' appeal and in opposition to plaintiffs' cross-appeal.

In Points I and IV below, defendants have set forth their reply argument in support of their appeal.

Commencing at page 19 and in Points V through VIII below, defendants have set forth their argument in response to the cross-appeal of plaintiff Transcontinental Oil Corporation ("Transcontinental") from dismissal of the first count of the complaint and the cross-appeal of plaintiff B. Edwin Sackett ("Sackett") from dismissal of the ninth and part of the tenth counts of the complaint.

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* Hereinafter sometimes jointly referred to as "the defendants".

I.

JUDGMENT SHOULD HAVE BEEN ENTERED IN FAVOR OF TRENTON ON THE FIRST AND SECOND COUNTERCLAIMS FOR PLAINTIFFS' WRONGFUL REFUSAL TO PERMIT TRENTON TO TRANSFER ITS SHARES

Upon assuming control of Transcontinental, plaintiff Sackett, in October 1966, caused Transcontinental's transfer agent to stop the transfer of all of Trenton's remaining shares on the specious grounds that the shares were "unregistered" (A282-383).

From 1966 to this very date, some eleven years, the plaintiffs have continued to refuse to permit Trenton to transfer its shares.* Notwithstanding Judge Conner's denial of plaintiffs' claim to Trenton's shares, the stop order remains in force and effect, all to Trenton's substantial damage.

Plaintiffs, under both the first and second counts of the complaint, sought a "permanent injunction enjoining and restraining Trenton from transferring any or all of the shares of Trans described in said Count" (A24).

The District Court denied plaintiffs the relief sought with respect to the Transcontinental shares which Trenton still owned. Nonetheless, plaintiffs (a) continue to prevent Trenton's transfer of its shares and (b) argue that Trenton is not entitled to recover damages resulting from the stop-order which was wrongfully placed upon its shares in 1966.

Judge Conner has concluded that Trenton was the rightful owner of the shares and has refused to grant to plaintiffs an injunction against Trenton's transfer of them. Nonetheless,

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* All in violation of the provisions of U.C.C. Sec. 8-401 and the authorities cited at pages 57 to 63 of defendants' main brief.

the District Court has incorrectly refused to assess damages against plaintiffs for their improper refusal to transfer Trenton's stock. Although a conversion of Trenton's shares has taken place, the District Court has erroneously denied to Trenton a remedy for the losses which it has suffered.

Both plaintiffs and the District Court have contended that plaintiffs' "good faith" or lack of "bad faith" or Sackett's "adverse claims" are all valid reasons for preventing Trenton from transferring its shares -- for eleven years!! The decision below is clearly erroneous and contrary to the authorities cited at pages 57 to 63 of the defendants' main brief. Trenton has been seriously damaged. It has won a lawsuit in which its right to the shares in question were attacked. Yet the District Court has improperly refused to compensate it for its damages.

Faced with adverse claims to Trenton's stock Transcontinental could have protected itself and Trenton by requiring the posting of an indemnity bond. It chose not to do so. Would not any prudent company, faced with an adverse claim to shares, require the posting of a bond, to protect itself against possible liability for a wrongful stop-order? Trenton is entitled to recover its damages from Transcontinental and Sackett resulting from the improper stop-order. If Transcontinental failed to protect itself from potential damages resulting from its acts, by requiring a bond from Sackett, that is Transcontinental's risk. It should not be the risk of Trenton. Trenton has been wronged and has suffered damages for which it should be compensated.

Plaintiffs could have, at the outset of this litigation, sought a preliminary injunction enjoining Trenton's transfer of its shares. To avoid (a) the possibility of being unable to obtain such a preliminary injunction and (b) the need to post a bond, Transcontinental and Sackett employed self-help and unilaterally stopped the transfer of Trenton's shares. By so doing, plaintiffs proceeded at their peril and should be compelled to compensate Trenton for the wrongful stopping of the shares.

Plaintiffs present a hodge-podge of excuses for the stop-order (Plaintiffs' Brief, p. 52-58). However, they admit that with respect to a large block of shares "Trans has not disputed Trenton's right to have acquired the so-called 'Trenton-Anglo Purchase Shares'". (Plaintiffs' Brief, p. 56). These are 150,000 shares which Trenton received from Anglo in 1960 in exchange for a 1/8th working interest in the Sedalia property. The only reason ever asserted below for the stopping of those shares was that Sackett had made an adverse claim to them. Thus, based upon Sackett's claim that he was entitled to "all" of Trenton's shares, and in the face of the clear terms of the June 22, 1966 agreement to the contrary, Transcontinental prevented Trenton's transfer of the "Trenton-Anglo Purchase Shares". Sackett's claim has been rejected but Trenton has not been compensated for the damages resulting from the conversion of its shares.

The District Court's refusal to sustain Trenton's counterclaims is clearly erroneous and establishes a dangerous precedent which should not be permitted to stand. A corporation must be accountable if it improvidently stops the transfer of a

shareholder's stock. This is especially the case, when, as here, it waits an inordinately prolonged period of time for a court determination of the propriety of its actions.* Were the law otherwise, a corporation and its management could act with virtual impunity to protect itself from corporate take-overs and the like. All that would be required is a colorable excuse to stop a transfer.

Had Transcontinental proceeded in good faith in 1966, it would have (i) required a bond to be posted to indemnify itself and Trenton against damages resulting from the improvident granting of the stop-order, or (ii) alternatively, attempted to obtain a preliminary injunction against Trenton's transfer of its shares, pending the determination of the action. In the latter case, an indemnity bond would have been required. Having failed to pursue either of the foregoing courses of action, Transcontinental has demonstrated that it was not acting in good faith.

Accordingly, defendants respectfully request that the District Court's dismissal of the first and second counterclaims be reversed and remanded for a trial on the issue of damages resulting from the wrongful stop-order.

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* Kanton v. United States Plastics, Inc., 248 F. Supp 353 (D.N.J. 1965), relied upon by plaintiffs, only recognizes the "good faith" of a corporation as an excuse for "temporarily refusing to register the transfer". A situation quite different from the case at bar.

II.

THE DISTRICT COURT'S DISMISSAL OF THE THIRD COUNTERCLAIM FOR VIOLATION OF SECTION 10(b) WAS CLEARLY ERRONEOUS AND CONTRARY TO LAW

Neither the plaintiffs, in their brief on this appeal, nor Judge Conner, in his decision below, have dealt with or responded to the primary thrust of defendants' counterclaim for violation of Section 10(b) of the Securities and Exchange Act of 1934 and Rule 10(b)5 promulgated thereunder. Defendant Trenton has proven (a) that plaintiffs together with those on behalf of whom Sackett acted wrongfully prevented Trenton's sale of its shares, commencing in October, 1966; and (b) that during the period of time that Trenton was prevented from selling its shares, (i) Transcontinental sold and distributed many millions of shares and (ii) Sackett and his group sold off some 174,668 shares.

Specifically, Transcontinental, while preventing Trenton's sales, made the following stock distributions (Exhibit UUUU, Transcontinental Annual Reports):

	Profit (Loss)	Total Debt	Unregistered New Shares Issued (Expressed in Shares Prior to 1 for 4 Reverse Split in 1968)
1967	($45,726)	$ 422,000	3,385,165
1968	($345,554)	$2,295,115	2,048,932
1969	($150,035)	$3,942,600	295,108
1970	($414,063)	$3,624,882	2,229,816
1971	($584,246)	$5,868,027	2,150,384
1972	$170,585	$7,195,147	2,148,592
TOTAL	($1,369,039)		12,259,997

It is apparent from the foregoing that the plaintiffs and the third-party defendants had a strong financial interest in

keeping Trenton's shares off the market where they would have been a depressing influence upon the price of Transcontinental's common stock and would have adversely affected plaintiffs' ability to engage in their massive stock distribution.

The wrongful prevention of stock sales by a company and those who control it, while selling and distributing their own shares, is both a tort and a violation of Section 10(b). Mariash v. Morrill, 496 F.2d 1138 (2d Cir. 1974); Rothberg v. National Banner Corporation, 259 F.Supp. 414 (E.D.Pa. 1966).

Plaintiffs' manipulation of the trading in Transcontinental, by stopping Trenton's sales, was an intentional wrong, regardless of motivation, for which Trenton should be compensated. Neither plaintiffs nor Judge Conner have come to grips with this issue. Had the District Court done so, it would have been compelled to render judgment for Trenton on the third counterclaim.

In addition to the foregoing, defendants, on their third counterclaim, established that Sackett and the additional defendants fraudulently induced Trenton into relinquishing its 650,000 shares of Transcontinental. In connection therewith, Trenton proved that Sackett and the additional defendants:

(1) made untrue statements of material facts when, prior to the execution of the June 22, 1966 agreement, defendants Trenton and Fein inquired of defendant Sackett acting on behalf of the additional defendants, as to whether Harry B. Leslie was one of the persons on behalf of whom Sackett was acting and

informed Sackett that Fein and Trenton would not sell their shares of Transcontinental to a group of purchasers which included Mr. Leslie because of Mr. Leslie's prior association with persons who had defrauded Transcontinental and with other persons with bad business reputations, including the infamous Lowell Birell; and in response to the aforesaid inquiry of Trenton and Fein, Sackett knowingly and falsely stated that defendant Leslie was not one of the persons on behalf of whom he was acting (Tr. 620-621).

(2) omitted to state that it was their intention, immediately after they gained control of Transcontinental, to unlawfully prevent defendant Trenton from selling and transferring its remaining shares of Transcontinental (a) in order to artificially manipulate the market price of the common stock of Transcontinental so that Transcontinental could distribute millions of shares of stock and so that Sackett and his group could sell their shares for higher prices and (b) in order to renegotiate with Trenton and Fein the terms of the June 22, 1966 agreement.

In reliance upon the foregoing fraudulent acts of Sackett and the additional defendants, Trenton entered into the June 22, 1966 agreement. Immediately after Sackett and the additional defendants acquired the 650,000 shares from Trenton, they combined their stockholdings in order to control the business and affairs of Transcontinental and have used their control to artificially control the market in the shares of Transcontinental by preventing defendant Trenton from selling or transferring its remaining shares, while permitting their own sales and Transcontinental's distribution, all to the damage of Trenton.

Plaintiffs, in their brief, carefully ignore the fact that Sackett's group was organized by Leslie, a close confederate of the notorious Lowell M. Birrell, and that the group consisted of mostly over-the-counter stock brokers. The identity of all of these persons and entities was a carefully guarded secret, with Sackett acting as their only disclosed principal. It is hardly surprising that once ensconced in control of Transcontinental, this group would proceed to attempt to manipulate the market in Transcontinental's stock.

Finally, it is apparent from the record, that had Fein and Trenton known that Leslie was involved with this group, they would have never relinquished control to Sackett's group. For it was Leslie who in 1959 brought Burkinshaw and Thomas Cairns, a confederate of Lowell Birell, into control of Transcontinental. From 1960 to 1965, Fein fought this group with his own money and ultimately succeeded in eliminating their influence in Transcontinental.

For all of the reasons stated above, judgment should have been rendered in favor of the defendants on the third counterclaim. Transcontinental and Sackett and his group should be compelled to compensate the defendants for the losses which they have suffered.

III.

THE SECOND COUNT OF THE COMPLAINT (THE DESILETS SHARES) SHOULD HAVE BEEN DISMISSED ON THE GROUNDS OF RES JUDICATA, COLLATERAL ESTOPPEL, RELEASE, LIMITATIONS AND ON THE MERITS

A. The Prior Adjudication, Between the Same Parties On The Same Claims and Issues, Bars the Second Count

(i) The Allegations of the Complaints Are The Same

Plaintiffs dispute Judge Conner's finding that "the complaints in the 1965 action and the case at bar reveals that the second count in this action substantially duplicates paragraph 22 of the 1965 complaint" (A122).

Plaintiffs' sophistry cannot explain away the clear allegations of the two complaints and their virtual identity.

1965 Complaint:

Plaintiffs, in the 1965 complaint attacked, the issuance of Transcontinental stock for inadequate consideration:

> 9. On or about January 1st, 1960, FEIN assumed control over the Board of Directors of TRANS and at all times thereafter the said FEIN has controlled the said Board of Directors. (A173)
>
> ....
>
> 22. From time to time, since on or about January 1, 1960 Fein had caused the stock of Trans to be issued at nominal, unfair and inadequate consideration to third parties whose names are not presently known to plaintiff, for the benefit of said defendant. Such issuance and sale of stock have been a waste of the assets of Trans.... (A176).

The following relief was sought (A178):

> (d) Enjoining the defendants and each of them from transferring, assigning, alienating, mortgaging or pledging any and all shares of stock unlawfully obtained by them since January 1st, 1960 or from voting any of such stock;
>
> ....

(e) Cancelling all shares of stock issued to the defendants or any of them or which, directly or indirectly, have unlawfully come into their ownership, possession or control since January 1, 1960.

....

(g) Impressing a trust upon all shares of stock of Trans or other property or assets improperly acquired by the defendants or any of them which this Court may determine to have been wrongfully misappropriated or diverted from Transcontinental.

1967 Complaint

In the 1967 complaint, plaintiffs made the same allegations relating to the issuance of stock in 1960, without consideration to Transcontinental (A12-13):

15. On or about the 12th day of April 1960, and while in control of TRANS, FEIN caused TRANS to authorize the issuance of 100,000 shares of the common stock of TRANS to one, Arthur A. Desilets.

16. On or about the 25th day of April 1960, the said 100,000 shares of stock were issued but on information and belief the said stock was never delivered by TRANS to the said Arthur A. Desilets, and remained at all times the property of TRANS and within the sole possession and control of FEIN.

17. On information and belief, the said 100,000 shares of stock were thereafter appropriated by TRENTON and FEIN to their own uses and purposes, and on or about the 5th day of August 1966, the said 100,000 shares were transferred by TRENTON and FEIN to divers persons, for the sole and exclusive benefit of TRENTON and FEIN, and entirely without any payment or remuneration to TRANS for said 100,000 shares of stock.

The foregoing allegations of the two complaints relate to the issuance by Transcontinental, while under the control of Fein, of stock for inadequate or no consideration. They amply support Judge Conner's conclusion that the "second count in this action substantially duplicates paragraph 22 of the 1965 complaint" (A122). For that reason alone, the second count should have been dismissed.

(ii) Judge Conner Erred in Refusing to Dismiss the Second Count on the Grounds of Res Judicata and Collateral Estoppel

Although conceding that the issues and claims alleged in the second count of the complaint were barred by res judicata (A122), the District Court improperly refused to dismiss this claim. The Court's ratio[illegible] for its refusal to dismiss the claim is based upon its co[illegible]sion that "plaintiffs altered their theory of recovery" in the pre-trial order of October 15, 1970 (A122). According to the Court, plaintiffs then claimed that the Desilets shares "belonged to the company" because they "were issued, pursuant to an April 12, 1960 resolution of the board of directors, without any consideration for their issuance" and are therefore "void" (A122-123). Since the shares "belonged to the company", the District Court concluded that defendants converted the shares when they transferred them to Fieland in mid-1966 (A123).

Plaintiffs contended and Judge Conner found that in 1960 the Desilets shares were issued "without any consideration" for their issuance (A122-123). On this appeal plaintiffs argue throughout that "there is nothing in the record to establish that any consideration was ever received by Trans for the issuance of such stock [in 1960]"; that the shares should "have been returned to the transfer agent" by the defendants; and that "the Desilets shares remained at all time the property of Trans" (Plaintiffs' Brief, p. 19-21).

Is this not the very claim alleged by plaintiff in paragraph 22 of their 1965 complaint?:

22. From time to time, since on or about January 1, 1960 Fein had caused the stock of Trans to be issued at nominal, unfair and inadequate consideration to third parties whose names are not presently known to plaintiff, for the benefit of said defendant. Such issuance and sale of stock have been a waste of the assets of Trans.... (A176).

If the Desilets transaction was not the subject of attack in the 1965 complaint, what transactions were under attack? Plaintiffs have never responded to this inquiry either below or on this appeal. The reason is obvious. The claim sought to be proven below was barred by the prior adjudication. At the least, the alleged claim that the issuance of the Desilets shares was "without consideration" is barred by collateral estoppel, since it is a claim "arising from, connected with or relating to" (A166) the matters alleged in the prior action. Certainly such claim "could have been asserted" (A166) in support of the allegations in the prior action. Accordingly, under both the complaint (which was never amended) and under the pre-trial order the claims and issues presented by plaintiffs are barred by res judicata and collateral estoppel.

B. The Statute of Limitations Bars the Second Count

Plaintiffs, and Judge Conner, urge that although the Desilets shares were issued "without consideration" in 1960 and were therefore "void", the alleged conversion did not take place until 1966 when defendants turned the shares over to Fieland (A123-124; Plaintiffs' Brief p. 46).

Neither the plaintiff nor Judge Conner have dealt with the applicability of the three year statute of limitations to the alleged conversion of the Desilets shares. C.P.L.R. § 214; Civil Practice Act § 49(7).*

* At point V subpoint E below defendants discuss at length the applicability of the three year statute of limitations for conversion to the first count of the complaint. The argument is equally applicable to the second count of the complaint.

Any attack upon the validity of the issuance of the Desilets shares in 1960 was clearly barred by 1967 when this action began. Judge Conner fully recognized this fact when he concluded that the conversion occurred in mid-1966 when the Desilets shares were delivered to Fieland. According to the Court, this "altered... theory of recovery" was first alleged in the pre-trial order filed on October 15, 1970. However, both the District Court and plaintiffs have failed to consider defendants' contention that the claim was time-barred when it was first alleged in the 1970 pre-trial order, more than three years after the claimed conversion. According to Judge Conner, under the 1970 pre-trial order, defendants were "no longer charged with any wrongful act in connection with the issuance of the stock" in 1960 (A122). This claim, as alleged in the complaint, would be barred by res judicata, as the District Court itself has acknowledged (A122). Instead, the District Court found that the pre-trial order of October 1970 charged defendants with converting the Desilets shares in mid-1966. However, by 1970 that claim was time-barred by the three year statute of limitations. Moreover, if the mid-1966 conversion claim is based upon different facts then the claim alleged in the complaint, there would be no relation back to the 1967 filing of the action. On the other hand, if the mid-1966 conversion claim is based upon the same facts as the claim alleged in the complaint, it would be barred by res judicata and collateral estoppel.* Under either conclusion the claim must be dismissed as barred either by limitations or by res judicata.

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*Defendants' position, as argued above, is that the claimed issuance of the Desilets shares in 1960, without consideration, is basic to plaintiffs' claim for conversion in this action and in the prior action. Accordingly, it is barred by the prior adjudication.

C. The Second Count of the Complaint Should Have Been Dismissed On The Merits

The Desilets shares were either "treasury shares" or shares which were recovered "from the former management and control" of Transcontinental and therefore Trenton was entitled to recover them under the letter agreement of August 13, 1960. (A217). Plaintiffs, on this appeal, ignore the clear provisions of the letter agreement. Their position is understandable since they stated in the pre-trial order of October 1970 that "Fein and Trenton misappropriated and converted 100,000 shares of Trans treasury stock, then standing in the name of one Arthur A. Desilets" (Emphasis supplied) (A60). Thus, at trial, there was no issue as to whether or not the Desilets shares were "treasury stock" since plaintiffs had previously admitted that fact. This admission has been totally ignored both by the plaintiffs and by Judge Conner in his opinion below. Having conceded that the Desilets shares were "treasury stock", plaintiffs cannot dispute that Trenton was entitled to them under the agreement of August 13, 1960.

At trial, defendants made no effort to prove that the Desilets shares were "treasury stock" since that fact had been conceded by plaintiffs. For the District Court to find against defendants on an issue which had previously been conceded by plaintiffs and against which defendants did not come to defend was manifestly unfair and clearly erroneous.

In addition, the District Court's conclusion that "having been illegally issued without consideration" the Desilets shares could never attain the status of treasury shares" (A123) is clearly erroneous.

First, the plaintiffs are barred, by res judicata and collateral estoppel from contending that the Desilets shares were

"issued without consideration" in 1960. Therefore, since the question of the propriety of the issuance of the Desilets shares has been previously adjudicated, plaintiffs should be precluded from urging that the shares are void and were not validly issued. Accordingly, since the Desilets shares were issued in 1960 by Transcontinental's transfer agent and the propriety of their issuance cannot be attacked, the District Court was compelled to conclude that the shares were treasury shares.

Secondly, as noted at pages 43-46 of defendants' main brief, Judge Conner's conclusion that the Desilets shares were issued "without consideration" is clearly erroneous and unsupported by the record. Judge Conner himself stated that the Desilets shares were issued "for reasons which remain unclear" (A91), thereby conceding that plaintiffs had failed in carrying their burden of proof.

Finally, under the letter agreement of August 13, 1960, Trenton was entitled to all shares recovered "from the former management and control" of Transcontinental. The Desilets Shares were issued during Burkinshaw's tenure and related to a deal which he brought to the company. After he was ousted the shares came back into the possession of the new management. Whether the Desilets shares were recovered from Burkinshaw, or from Anglo, or from Desilets is irrelevant. In Judge Conner's words, Desilets was one of Burkinshaw's "fronts" and recovery of the shares from him is equivalent to recovering the shares "from the former management." Accordingly, under the terms of the letter of August 13, 1960, Trenton was entitled to receive the Desilets shares. Trenton's transfer of the shares to Fieland in 1966 was, therefore, not a conversion of an asset belonging to Transcontinental. The decision of the District Court to the contrary was clearly erroneous.

IV.

PLAINTIFFS FAILED TO PROVE DAMAGES ON THE SECOND COUNT AND THE MEASURE OF DAMAGES FIXED BY THE DISTRICT COURT IS CLEARLY ERRONEOUS

In attempting to prove damages resulting from the alleged conversion of the Desilets shares plaintiffs made no attempt to prove actual transactions in Transcontinental stock. Since such proof was available, the District Court's use of alleged bids and offers for 100 shares as reflected in a report of the National Quotation Bureau was error.

Apparently recognizing this infirmity, plaintiffs again rely upon arguments properly rejected by the District Court. First, the District Court rejected "plaintiffs belated attempt in its reply brief to rely upon ostensible sales made by Fieland and referred to in a state court complaint" (A154). The complaint was introduced into evidence to impeach Fieland's testimony "not as proof of the facts asserted therein" (A152).

Secondly, the District Court rejected plaintiffs' contention that the answer and counterclaims filed by defendants in 1967, alleging damages of 70¢ per share was "too remote in time" to serve as proof of fair market value in October 1966 (A153).

The District Court also held that the delivery to Fieland of 70,000 shares in lieu of a $35,000 attorney's fee owed to him did "not provide persuasive proof of the fair market value of Trans stock" (A153) since "this was not the type of routine, arm's length transaction upon which a court may base a finding of fair market value."

With due respect to the District Court, the alleged bid and asked price for 100 shares of a penny stock, as reflected by the National Quotation Bureau is also "not the type of routine, arm's length transaction upon which a court may base a finding of fair market value" for 100,000 shares. As defendants expert, Robert Martin, the only witness on this point, testified, the quotations do not reflect actual trades. At best, they are reported bids and offers for 100 shares and, at worst, they are statements from brokers attempting to ascertain whether there was any public interest in buying or selling Transcontinental stock (12/8/75 Tr. 28).

Plaintiffs chose not to present proof of actual sales. Having done so, it was clearly erroneous for the District Court to have relied upon the highly suspect proof which was presented.

Since proof of actual 1966 transactions (e.g., Transcontinental's October 1966 issuance of debentures convertible into common stock at $.25 per share) was available, it was error for the District Court to ignore it in favor of an unconfirmed "asked" price of 44¢ per share. For this reason alone, and for all of the reasons set forth in Defendants' Main Brief at pages 47 to 54, the District Court's conclusion that the fair market value of 100,000 Transcontinental shares in 1966 was $.44 per share was clearly erroneous.

Finally, the District Court found that Transcontinental was entitled to recover "the amount of any proceeds received by Fein upon his sale of the Desilets stock" (A155-156). This claim was never asserted by plaintiffs in the complaint, the pre-trial order or their post-trial memorandum on damages. This post-trial

theory is entirely the product of the District Court. It was never raised by plaintiffs at trial. Defendants, therefore, never had an opportunity to defend against it or to prove (i) "that Fieland was discounting his claim" and (ii) the amount which "properly should be attributed to the Fieland transaction." (A156).

Plaintiffs have not and cannot defend this obvious error of the District Court. Accordingly, the decision on damages should be reversed.

The Facts Relevant To Plaintiffs' Cross-Appeal

The Findings of Fact set forth in detail in Judge Conner's opinion on the issue of liability clearly support the District Court's conclusion dismissing the first, ninth and tenth counts of the complaint. Indeed, at no point in their brief do the plaintiffs attack Judge Conner's Findings of Fact as unsupported by the record and none are urged to be clearly erroneous. The District Court's factual conclusions, which in relevant part are set forth below, support the dismissal of the aforesaid counts of plaintiffs' complaint.

Findings of Fact

In the late 1950's, Harry B. Leslie ("Leslie"), a New York stock broker, with some assistance from defendant Fein, one of his customers, engaged in a successful proxy fight to wrest control of Transcontinental from a group related to Virginia Iron, Coal & Coke Company ("Virginia Iron"), headed by one Samuel Brown ("Brown") (A86).

Leslie asked Fein to become president of Transcontinental until he could find someone familiar with the oil industry (A86). After Fein became president, he discovered that prior management had looted the company (A87). Transcontinental's claims against Virginia Iron were settled by Virginia Iron purchasing all of Transcontinental's wells for $550,000 cash and by the return of certain shares of stock, in Brown's name, to the treasury of Transcontinental (A). After the cash was used to pay off the holders of Transcontinental's convertible debentures, the company was left with $55,000 of U.S. treasury bonds and a tax loss (A87).

About a year later, Leslie introduced Fein to Messrs. Orville V. Burkinshaw ("Burkinshaw") and Thomas Cairns ("Cairns") who were the principals of a Canadian company, Anglo-Pacific Oil and Gas, Ltd. ("Anglo") (A 87).

To take advantage of Transcontinental's tax loss carry-forward, Burkinshaw and Cairns proposed that, in exchange for 1,000,000 shares of Transcontinental's common stock and other

consideration, Transcontinental acquire from Anglo all the outstanding stock of the White River Exploration Company, which was the owner of certain oil fields in Rangely, Colorado ("the Rangely property") (A87).

The proposal was accepted and embodied in a written agreement dated October 1, 1959 and on or about February 5, 1960 1,000,000 shares of stock of Transcontinental were issued to Anglo, in care of Burkinshaw (A88).

As a result of this transaction, Anglo acquired full management and control of Transcontinental. Fein resigned as president of Transcontinental effective November 30, 1959 and Burkinshaw was elected in his place. Furthermore, Burkinshaw and his Anglo associates assumed a majority of the seats on the board of directors of Transcontinental and all of its executive positions. The books and records of the corporation were removed to Anglo's Canadian offices (A88).

During the tenure of Burkinshaw's group, the possibility of acquiring certain shut-in oil and gas wells in Sedalia, Alberta, Canada ("the Sedalia property") was explored. Since Transcontinental was unable to secure the requisite financing on its own, Burkinshaw arranged with Fein to raise the needed funds. Fein in turn went to Bernard Green ("Green"), a Trenton, New Jersey lawyer who, together with a number of his clients and a Doctor A. Arthur Weiss, undertook to finance the Sedalia deal (A88-89).

This group, which formed Trenton for the purpose, raised $225,000. Fein added $17,000 of his own and the total of $242,000 was lent to Transcontinental pursuant to a loan agreement dated April 11, 1960 (A89).

In return, Trenton received Transcontinental's note for $242,000, a security interest in the Rangely property, 150,000 shares of original issue Transcontinental stock ("the Original Issue shares") and a three-eighths working interest in the Sedalia property (A89).

Anglo, which also wished to participate in the Sedalia deal, entered into an agreement with Trenton whereby Anglo received one-third of Trenton's three-eighths working interest in the Sedalia property in exchange for 150,000 shares of the 1,000,000 shares of Transcontinental stock which Anglo had acquired from Transcontinental in the Rangely deal (the "Anglo-Trenton shares").*

Subsequently, Green expressed his understanding that Trenton was entitled to receive from Transcontinental 150,000 freely transferable shares rather than newly issued, unregistered stock. Apparently recognizing the validity of this claim, Transcontinental's board of directors, on May 27, 1960, authorized the issuance to Trenton of 141,000 treasury shares ("the Brown shares") and 9,000 original issue shares in place of the 150,000 Original Issue shares which had been previously issued to Trenton.

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* At no time in the proceedings below did Transcontinental question the propriety of Trenton's receipt of the Anglo-Trenton shares. The purported reason for a stop-order being placed against these shares was the existence of Sackett's "adverse claim" to them.

After the Sedalia deal was closed, it was discovered that 25 per cent of the Rangely property, which had been pledged as security for Trenton's $242,000 loan to Transcontinental, had previously been assigned by Burkinshaw to third parties; that Burkinshaw had overstated the purchase price for the Sedalia property by $65,000; and that he had misappropriated all but $10,000 of this difference (A94-95).

Upon learning of these acts, Green, who was Trenton's president, threatened to call the note and throw Transcontinental into bankruptcy (A95).

In order to forestall and appease Trenton, the following steps were taken (A96-97):

1) Burkinshaw and his group surrendered control of Transcontinental;

2) Green and his law partner, Robinson, were elected to Transcontinental's board of directors;

3) Fein resumed the presidency of the company;

4) Fein as president of Transcontinental, delivered to Trenton a letter dated August 13, 1960, stating in relevant part:

> The following summarizes our understanding on the situation involving the default on the loan of $242,000 by us from Trenton Products.
>
> 1. Trenton Products has failed to receive the security provided for in the loan agreement. The prior management of this company fraudulently transferred such assets to others in violation thereof.
>
> 2. Trenton Products will support the management of this company in any litigation to secure the return of such assets. If successful therein, such assets will be transferred to Trenton Products to further secure its loan.
>
> ....

4. Trenton Products shall be entitled to receive from us, such additional shares of our company as we are able to recover from the former management and control of the company, together with such shares as may be held in the Treasury of the company, as partial recoupment of the damages sustained by you arising out of the failure of this company to perform its obligations, and without further obligation. While it is recognized that such shares have no value at this time due to the condition of the company, it is hoped that forebearance by you may result in this company being restored to viable condition in the immediate future.

5. We concede the insolvency of this company at this time. Nevertheless, it is our understanding that so long as we cooperate with you, that you will forego any effort to collect the $242,000 owed to you at this time with interest, and that you will cooperate in an effort to keep this company alive.

Notwithstanding the foregoing efforts to placate Trenton, many Trenton investors insisted upon being repaid. As a result, Fein personally repaid a substantial sum of money to those Trenton investors who no longer wished to continue their investment (A97).

Between the time of the Trenton $242,000 loan to Transcontinental in April 1960 and Burkinshaw's ouster in August 1960, additional improprieties came to light. In about May 1960, while Burkinshaw was still in control of Transcontinental, Fein sent an accountant to Calgary, Canada, where Transcontinental's offices had been relocated, to examine the company's books and records. There it was discovered that the $55,000 in United States treasury notes, Transcontinental's sole liquid asset, had been embezzled, thereby leaving the company without any funds (A97).

As partial restitution, Burkinshaw caused Anglo to issue a demand note to Transcontinental for $39,043.50 secured by 500,000 of the 1,000,000 Transcontinental shares which Anglo had acquired in the Rangely deal (A97).

After the removal of Burkinshaw from control of Transcontinental, Anglo, after demand, defaulted in payment of the $39,043.50 note (A98). As a result, after notice to Anglo, the security for the note (i.e., the Transcontinental stock) was sold, at a private sale, to Trenton for $10,000 on March 20, 1961 (A98).

In addition, and also after Burkinshaw's ouster, Anglo, on August 17, 1960, returned to Transcontinental's attorneys 350,000 shares of Transcontinental stock, representing the remainder of the 1,000,000 shares it had received in the Rangely deal (A98). Of these shares, 300,000 were thereupon delivered to Transcontinental and Fein (A99).

The financial difficulties of Transcontinental resulting from Burkinshaw's frauds were further aggravated when, in 1960, the income from Transcontinental's sole revenue-producing property, the Rangely fields, was withheld as the result of litigation pending against Transcontinental in Colorado. On October 13, 1961, an order was entered in the District Court of Colorado appointing a Receiver of the income from the Rangely property. The receivership continued until December 14, 1964, when the Court entered an order discharging the Receiver and dismissing the action (A100).

During this entire period, between 1961 and 1964 inclusive, Transcontinental was entirely without any source of income (A100).

As a result of Transcontinental's failure to pay its bills, its stock transfer agent, the Texas Bank & Trust Company, ceased performing services for Transcontinental and refused to relinquish the company's records. Fein, and his secretary Theresa Zappley, were therefore required to assume the duties of transfer agents (A100).

It is undisputed that during this entire period Trenton and Fein lent substantial sums of money to Transcontinental to help pay its bills (A100).*

The receivership of the Rangely, Colorado property was removed in 1965. Notwithstanding the lifting of the receivership, Transcontinental "remained a financial disaster"(A101). As described by plaintiffs' counsel in a 1966 affidavit, the corporation was "without funds, faced with bleak financial prospects, burdened with debt" and in a "dormant and moribund state" (A101).

Shortly after the litigation in Colorado was terminated, Sackett commenced two lawsuits against Transcontinental and its directors. In the Court of Chancery, Delaware, Sackett sought an

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* Moreover, although Fein was to receive an annual salary of $10,000 per annum, because of Transcontinental's insolvency, Fein received no compensation for six years, from 1960 to 1966, when he relinquished control to Sackett. During this six year period, the company had no salaried employees. Since Fein was the president of another public company, he had available to him both a secretary and an office out of which he could attend to Transcontinental's affairs. The company paid nothing for these services.

order requiring Transcontinental to hold an election of directors. In this Court he commenced Sackett v. Transcontinental, 65 Civ. 2500 (S.D.N.Y.), charging breaches of fiduciary duty and various malfeasances and nonfeasances (including stock conversions) on the part of Fein and Trenton between 1960 and 1965 (A101-102). Specifically, the complaint charged Fein with having caused the stock of Transcontinental to be issued at nominal, unfair and inadequate consideration to third parties for his own benefit; and that Fein caused large quantities of the issued and outstanding stock of Trans to be purchased for his own benefit under such circumstances that the acquisition of said stock should have been for the benefit of Transcontinental. Plaintiff demanded judgment enjoining defendants Fein and Trenton from transferring all shares unlawfully obtained by them since January 1, 1960 and cancelling such shares (A102).

After several months of negotiations, the two actions were settled. A final judgment approving the settlement as fair and adequate was entered in the Southern District by Judge Tyler on July 12, 1966. The settlement was based upon a stipulation, specifically approved by Judge Tyler, consenting to a dismissal of the complaint,

> "with prejudice, against Trans, its successors and assigns and its stockholders, with respect to all claims or causes of action arising from, connected with or related to any of the matters or transactions alleged in the complaint * * * or which could have been asserted thereunder."

In addition, general releases, containing essentially the same language, were executed by Transcontinental and delivered to Fein and Trenton (A103).

Pursuant to the stipulation approved by the Court, the case was settled on the following terms:

1) Fein released a claim for six years of unpaid salary, amounting to approximately $60,000;

2) Fein agreed to deliver a general release executed by Louis Fieland ("Fieland") releasing Fieland's $35,000 claim for legal fees against Transcontinental*;

3) Fein's group agreed to surrender management of the corporation to Sackett's group;

4) Sackett agreed to effect the discontinuance of the Delaware action;

5) Fein waived any claim for legal fees or other expenses incurred in defending the lawsuit;

6) Transcontinental agreed to deliver a general release (A103-104).

In conjunction with the settlement, and expressly contingent thereon, an agreement dated June 22, 1966 ("the June 22, 1966 agreement") was entered into between Trenton and Sackett for himself and "as nominee" for undisclosed others whereby:

1) Trenton would transfer to Sackett all its right, title and interest in (a) 650,000 shares of the common stock of

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* Fieland was an attorney who had, during the 1960's, represented Transcontinental in extensive litigation with Anglo, which resulted in an uncollected judgment of in excess of $600,000.

Transcontinental which it owned of record and/or beneficially, (b) the remaining $225,460.72 of the loan Trenton had made to Transcontinental to finance the Sedalia deal, (c) the security therefor, and (d) Trenton's two-eighths interest in the Sedalia property;

2) Sackett agreed to pay Trenton $187,500;

3) Trenton and Fein warranted, among other things, that to the best of their actual knowledge the outstanding stock of Transcontinental consisted of not more than 3,600,000 shares of common stock;

4) Damages for breach of the above warranties was not to attach unless the damages arising from all such breaches exceeded $10,000, in which case the total damages recoverable were to be limited to $10,000 (A104-105).

On August 12, 1966, Fein and Sackett and their respective attorneys met and closed the June 22, 1966 agreement. Among other things, 650,000 shares of Transcontinental stock were delivered to Sackett (A105).

Within two months of assuming control, and on October 6, 1966, counsel for Transcontinental, upon instructions from Sackett, the new president of Transcontinental, directed the company's transfer agent to stop the transfer of all of the remaining shares of Transcontinental still owned by Trenton or transferred by Trenton to third parties on the grounds that the shares were "unregistered" (A106-107).

Although the stop order was applied to all shares held by Trenton or which had been transferred by Trenton to third parties (e.g., Fieland, Weiss, Herzfeld & Stern), no restrictions were placed upon the transferability of the shares Sackett's group had acquired from Trenton, although under the theories propounded by plaintiffs at trial, those shares are rightfully the property of Transcontinental (A107).

Trenton has charged that the stop order placed upon its shares (and still in effect) constituted an unlawful conversion of its shares for which damages are sought (A108).

V.

THE FIRST COUNT OF THE COMPLAINT FOR ALLEGED 1960 AND 1961 STOCK CONVERSIONS WAS PROPERLY DISMISSED

A. Preliminary Statement: The Unfairness of the Proceedings Below

In the first count of the complaint, filed in 1967, plaintiff Transcontinental alleged that "on or about the 17th day of August, 1960, Anglo-Pacific agreed to return to Trans and did there and then deliver to Trans 300,000 shares of the 1,000,000 shares theretofore delivered by Trans to Anglo-Pacific " (A12); and that thereafter, "Trenton and Fein appropriated the said 300,000 shares of Trans stock to their own uses and purposes " (A12).

In the pre-trial order, entered in 1970, after the conclusion of three years of discovery, plaintiffs reiterated that the first count of the complaint related to the alleged conversion by defendants of the aforesaid 300,000 shares of Transcontinental stock (A60). The pre-trial order further stated that the parties agreed that the trial of the action was to "be based upon this order and upon the pleadings as amended" (A52). Thus, in accordance with Rule 16 of the Federal Rules of Civil Procedure, a pre-trial order was entered "which limits the issues for trial" to those set forth therein. Notwithstanding these clear strictures, at the trial of the action, plaintiffs were permitted to roam far afield. Numerous other stock transactions which took place 14 years earlier, were questioned for the first time. Indeed, not until plaintiffs filed their post-trial brief did it become apparent that they claimed, under the first count,

that defendants had converted 900,000 shares of Transcontinental stock in 1960 and 1961.

The transactions attacked included those relating to the August 17, 1960 Shares (250,000), the Collateral Security Shares (500,000) and the Original Issue Shares (150,000).* At trial, plaintiffs did not move to amend the complaint or the pre-trial order to expand the scope of the first count from an attack upon one 300,000 share transaction to an attack on three transactions totalling 900,000 shares. Under all of these circumstances, plaintiffs attempts to go beyond their pleadings was unfair, and should not have been permitted. After seven years of litigation, the defendants were required to meet, for the first time at trial, claims never before raised, relating to transactions fourteen years old. Defendants were thus deprived of a fair opportunity to defend plaintiffs' charges, which was manifestly unjust. Thomas v. E. J. Korvette, Inc., 476 F. 2d 471 (3rd Cir. 1973); Monod v. Futura, Inc., 415 F.2d 1170 (10th Cir. 1969); Case v. Abrams, 352 F.2d 193 (10th Cir. 1965).

Notwithstanding the foregoing, the District Court dealt with and dismissed all of plaintiffs' claims under the first count. We will discuss each of the transactions which plaintiffs sought to attack below, in the order in which they were disposed of by the District Court, and show how each is without merit and barred by the principles of res judicata, collateral estoppel, release and limitations.

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* Apparently recognizing that Sackett received many of these shares from Trenton when he acquired the 650,000 shares, plaintiffs on this appeal and for the first time are now apparently limiting their claim on the first count to 450,000 shares. This is but another example of plaintiff's continual change of claims and theories throughout this litigation.

B. The August 17, 1960 Shares (250,000) Shares*:

(i) The Claim Was Correctly Found to be Without Merit

Plaintiffs do not dispute that, while Burkinshaw was in control of Transcontinental, and on April 11, 1960, the company borrowed $242,000 from Trenton in order to finance the Sedalia deal (A89). Furthermore, it is uncontested that Transcontinental and Burkinshaw had defrauded Trenton in connection with the loan (A94-95).

To placate Trenton and its president Green and to forestall certain bankruptcy for Transcontinental, Burkinshaw and his group surrendered control of the company, Green and his partner were elected to the Board of Directors and Fein resumed the presidency (A96-97). Moreover, on August 13, 1960 Fein, as president of Transcontinental, delivered to Trenton a letter which stated in pertinent part (A17):

> 4. Trenton Products shall be entitled to receive from us, such additional shares of our company as we are able to recover from the former management and control of the company, together with such shares as may be held in the Treasury of the company, as partial recoupment of the damages sustained by you arising out of the failure of this company to perform its obligations, and without further obligation. While it is recognized that such shares have no value at this time due to the condition of the company, it is hoped that forebearance by you may result in this company being restored to viable condition in the immediate future.
>
> 5. We concede the insolvency of this company at this time. Nevertheless, it is our understanding that so long as we cooperate with you, that you will forego any effort to collect the $242,000 owed to you at this time with interest, and that you will cooperate in an effort to keep this company alive. (A17)

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* Presumably these are the "300,000 shares" which are referred to in the first count of the plaintiffs' complaint (A11-12).

Immediately after the ouster of Burkinshaw and the delivery of the foregoing letter and on August 17, 1960, Anglo returned to Transcontinental 300,000 shares of its Transcontinental stock (A98-99).*

Under Transcontinental's letter agreement of August 13, 1960 with Trenton, these shares immediately became the property of Trenton as shares which Transcontinental was able to recover "from the former management and control of the company" (A217).

Plaintiffs do not contest the fact that Burkinshaw and Transcontinental had defrauded Trenton. Instead, they chose to ignore the efforts made by both Fein and Trenton to save the company. As Judge Conner recognized, the delivery by Transcontinental to Trenton of the letter agreement of August 13, 1960, together with the delivery of all shares which could be recovered from Burkinshaw and Anglo was the only reasonable thing that Fein could have done to avoid the total collapse of Transcontinental. The business judgment he exercised fourteen years earlier cannot be assailed by plaintiffs. For had not Fein been able to keep the corpse alive, through great personal expense and effort, plaintiffs would not have later been able to reap the substantial profits which they have obtained through the vehicle of Transcontinental.

In dismissing Transcontinental's claim to the aforesaid shares, Judge Conner correctly concluded (A112-113):

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* We have referred to these shares as the August 17, 1960 shares as did Judge Conner in his decision below (A111). In the complaint plaintiffs claim that these shares were delivered by Anglo to Transcontinental on August 17, 1960. However, plaintiffs, in their brief refer to these shares as the "August 12, 1960 Agreement Shares" No "agreement" of August 12, 1960 was ever proven by plaintiffs and none ever considered by Judge Conner.

> The simple fact is that Trenton was a defrauded creditor who could have taken action which would probably have thrown Trans into bankruptcy. Its agreement to settle for, among other things, any stock which Trans might recover from Anglo seems eminently reasonable and even charitable. Indeed, this agreement so dissatisfied some of the Trenton shareholders that Fein felt constrained to buy them out at considerable personal expense.
>
> I accordingly find that the letter agreement of August 13, 1960 was not the product of bad faith or even bad judgment on the part of Fein and is enforceable. Thus, the acquisition of the August 17, 1960 shares by Trenton, pursuant to the express terms of the agreement, was a legal acquisition and any claim by Trans with respect to those shares is dismissed.

The District Court's dismissal of this claim was correct and fully supported by the record.

(ii) The Claim is Also Barred By the Principles of Res Judicata, Collateral Estoppel and Release

In dismissing this claim on the merits, Judge Conner did not pass upon the defenses of res judicata, collateral estoppel and release. Had he done so, he would have been compelled to uphold these defenses as a complete bar to the claim.

Plaintiffs contend that the shares delivered on August 17, 1960 by Anglo to Transcontinental "became the property of Trans" and should not have been acquired by the defendants (Plaintiffs' Brief p. 30).

In the prior derivative action settled in 1966, the complaint alleged, at paragraph 23, that between 1960 and 1965, Fein had acquired "large quantities of the issued and outstanding stock of Trans under circumstances where the acquisition of said stock should have been for the benefit of Trans instead of for his own benefit". (A176-177).

Judgment for money damages and other relief, including the following was sought (A178):

(d) Enjoining the defendants and each of them from transferring, assigning, alienating, mortgaging or pledging any and all shares of stock unlawfully obtained by them since January 1st, 1960 or from voting any of such stock;

....

(g) Impressing a trust upon all shares of stock of Trans or other property or assets improperly acquired by the defendants or any of them which this Court may determine to have been wrongfully misappropriated or diverted from Transcontinental.

The instant claim that on or about August 17, 1960 defendants wrongfully acquired Transcontinental stock, which stock allegedly belonged to the company, was covered by the 1965 complaint.

Fourteen years after August 17, 1960 and eight years after settlement of the 1965 derivative action, plaintiff's sought to again litigate a claim which had been adjudicated in 1966. The stipulation of settlement of the prior action, approved by Judge Tyler specifically dismissed "with prejudice...all claims or causes of action arising from, connected with or related to any of the matters or transactions alleged in the complaint... or which could have been asserted thereunder." In addition, Trenton and Fein obtained releases to the same effect (A201-204).

Accordingly, for all of the above reasons the claim relating to the August 17, 1960 shares should have been dismissed

as barred by the principles of res judicata, collateral estoppel and release.*

C. The Collateral Security Shares (500,000 Shares)**:

(i) The Claim Was Correctly Found to be Barred By The Prior Adjudication

As previously noted, after Fein had discovered that Burkinshaw had embezzled funds from Transcontinental, Anglo issued its demand note, in the amount of $39,043.50, to Transcontinental secured by 500,000 shares of Transcontinental stock ("The Collateral Security Shares"). After Burkinshaw's removal, Transcontinental was totally without funds. Whatever income it had from its sole revenue-producing property, the Rangely fields, was withheld as a result of litigation pending against the company in Colorado (A99-100). Accordingly, the company was insolvent, without funds, without income and unable to pay any of its current expenses (A100).

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* With respect to the August 17, 1960 shares and each of the allegedly converted blocks of stock, plaintiffs made no response, by way of proof, to the defenses of res judicata, collateral estoppel and release. If the instant claims are different from those in the prior action, why did plaintiffs fail to present any proof as to the nature of the transactions for which they previously sued? What transactions were they attacking in paragraphs 22 and 23 of their prior complaint? Those paragraphs contain broad and sweeping allegations of improper issuances and acquisition of Transcontinental stock. If they were not the same transactions tried below, then what transactions were they? What were the alleged wrongs which defendants settled? Plaintiffs' total failure to answer these questions at trial demonstrated that all of their claims were the same as those previously adjudicated.

** This claim is not alleged in the complaint nor in the pre-trial order, nor have the pleadings ever been amended to include this claim.

During this time, and on September 1, 1960, demand was made upon Anglo for payment on the $39,043.50 note (A231-232). When Anglo defaulted, Transcontinental, in desperate need for cash, held a private foreclosure sale at which Trenton purchased the shares for $10,000. The money was thereupon used by Transcontinental to aid it in paying its debts and expenses.

Judge Conner found that the claim by Transcontinental to the collateral security shares was barred by res judicata (A113-116):

> In this case, Fein is charged with having conspired with Trenton to purchase for their own benefit and for inadequate consideration 500,000 shares of Trans stock which Trans had the right to acquire for itself. This falls squarely within the allegations of paragraph 23 of the complaint in the 1965 action.

Paragraph 23 of the earlier complaint charged that Fein (A176-179):

> caused to be purchased large quantities of the issued and outstanding stock of TRANS under circumstances where the acquisition of said stock should have been for the benefit of TRANS instead of for his own benefit.

On the basis of the foregoing, Judge Conner, in dismissing the claim, stated (A117-118);

> I therefore conclude that any claim Trans may have against Trenton or Fein with respect to the Collateral Security shares is barred as being identical to or at least 'arising from, connected with or relating to' [A166] the matters alleged in the prior action; certainly such claims 'could have been asserted' [A166] in support of the allegations in the prior action.

The decision of the District Court is correct and should be affirmed. Plaintiffs have not and cannot demonstrate that the dismissal of this claim was clearly erroneous.

(ii) The Claim Is Also Without Merit

At trial, plaintiffs urged, for the first time, that the Collateral Security Shares were sold upon foreclosure at an inadequate consideration. Plaintiffs had never raised this issue in the complaint or the pre-trial order and therefore should not have been permitted to proceed. Nevertheless, the court permitted plaintiffs' attempts to prove a claim of inadequate consideration. Plaintiffs failed in their burden of proof. First, Trenton had an absolute right to obtain those shares pursuant to the letter agreement of August 13, 1960. Instead, in order to fully cut off any claim of Anglo to those shares (Tr. 885-901), a foreclosure sale was held and Trenton paid $10,000 to Transcontinental to aid it in payment of its debts and expenses. Fourteen years after the transaction, plaintiffs attempted, for the first time, to attack the adequacy of the foreclosure sale.

The proof presented at trial thus supported defendants position that Trenton had rightfully acquired the Collateral Security Shares. After due and proper notice to Anglo of default on its note (A231-232], the shares were sold on March 22, 1961 for $10,000. Plaintiffs concede that this sale took place at a time when Transcontinental "was without a ready source of income and required monies to pay for expenses then being incurred." (Plaintiff's Brief, p. 29). Moreover, there was nothing secretive about the foreclosure sale. Notice went to Anglo (A 231-232). Trenton received a Bill of Sale (A215). Anglo never attacked the sale and Transcontinental had no standing to attempt

to do so. Moreover, Trenton had an absolute right to receive those shares, without payment, pursuant to the letter agreement of August 13, 1960.

Judge Conner, recognizing the merits of defendants' position, noted in his opinion that had Transcontinental acquired the collateral security shares (A117):

> Trenton would have become entitled to such shares pursuant to the terms of paragraph 4 of the August 13, 1960 agreement (Finding 48). If this course had been taken, of course, Anglo's obligation on the note would have been wiped out. On the other hand, a proper foreclosure sale would leave Anglo indebted to Trans for any deficiency. If anyone was entitled to complain about the foreclosure sale, it was Anglo. But Anglo's own conduct had been so atrocious that it was not in a position to complain about anything, and it did not. Burkinshaw was obviously happy to use his acquiescence to buy himself freedom from prosecution.

Transcontinental's claim to the collateral security shares is, therefore, totally without merit.

D. The Original Issue Shares (150,000):

(i) The Claim Was Correctly Found to be Without Merit

In 1960 Transcontinental held 150,000 shares of its stock in its treasury. These shares, ("The Original Issue Shares") were delivered to Trenton pursuant to the terms of the letter agreement of August 13, 1960 which provided: "Trenton Products shall be entitled to receive from us... such shares as may be held in the Treasury of the company..." The shares were turned over to Trenton as partial compensation for the frauds which Burkinshaw and Transcontinental had committed in obtaining the $242,000 loan from Trenton (Tr. 678-695; 762-765).

Plaintiffs apparently do not attack Trenton's right to obtain from Transcontinental shares which were in the treasury of the company. Rather, plaintiffs take issue with the District Court's conclusion that the shares in question were treasury shares. The District Court's holding was entirely correct and should be sustained. The universally accepted definition of treasury shares are shares which a corporation has issued but which are not outstanding in the hands of a holder and which have not been "retired or cancelled or restored to the status of unissued shares." Ballentine, Corporations (rev. ed. 1946) § 260, at 614-615; Winkelman v. General Motors Corporation, 44 F.Supp. 960, 994-95 (S.D.N.Y. 1942).

The Original Issue shares come squarely within that definition. Plaintiffs' concede that pursuant to a Board of Directors resolution of April 12, 1960, 150,000 shares were validly issued to Trenton in partial consideration for Trenton's $240,000 loan. There is no dispute that the transfer agent thereafter issued certificates for those shares.

Some six weeks later, on May 27, 1960, at the request of Bernard Green of Trenton, Transcontinental's Board amended its prior resolution and authorized the issuance of 141,000 treasury shares (the Brown shares) and 9,000 new issue shares to Trenton in exchange for the Original Issue Shares. Although Trenton returned the Original Issue Shares to Transcontinental, those shares were never cancelled and were held by Transcontinental.

Thereafter, the fact that Burkinshaw and Transcontinental had defrauded Trenton in connection with the Sedalia property came to light. To appease Trenton and to save the company from sure bankruptcy if Trenton sought recission, the letter of August 13, 1960 was furnished to Trenton by Transcontinental promising, among other things, to give Trenton all of Transcontinental's treasury shares and all shares recouped from Anglo and the former management. Thus, the certificates representing 150,000 Original Issue shares which had originally been validly issued, but which had not been "retired or cancelled or restored to the status of unissued shares", and were thus treasury shares, were delivered to Trenton.

Plaintiffs persistently contend that the 150,000 Original Issue Shares should have been cancelled and therefore should not have been given to Trenton under the letter agreement of August 13, 1960. In fact, the shares had not been cancelled. Thus, they remained treasury shares of Transcontinental. Accordingly, Trenton was entitled to receive those shares pursuant to the letter agreement of August 13, 1960.

In rejecting plaintiffs' claim as being without merit, Judge Conner noted (A119):

> Upon their reacquisition by Trans, the Original Issue shares became treasury stock -- i.e., issued for consideration, subsequently reacquired by the corporation and retained uncancelled. Ballentine on Corporations 614-15 (Rev. Ed.1946). In effect, all that transpired as a result of the May 27, 1960 resolution was an exchange of stock, whereby the Original Issue shares were substituted as treasury stock in place of other treasury stock -- the Brown shares -- which had been delivered to Trenton.

> When Trenton subsequently became entitled to these shares pursuant to the August 13, 1960 letter agreement (Finding 48), Trans was in no worse position than if the exchange had never taken place. Trenton would have acquired the Brown shares in the same fashion if they had remained in the treasury.

The District Court's conclusion is both factually and legally correct and should not be disturbed.

(ii) The Claim Was Correctly Found to be Barred By Res Judicata

In addition to dismissing the claim on its merits, Judge Conner also ruled that the claim was barred by the doctrine of res judicata (A119).

Since the claim was never asserted in the complaint or in the pre-trial order, the District Court and the defendants were required to glean the full nature of plaintiffs' claim from plaintiffs' post-trial brief. In that brief, and in plaintiffs' brief on this appeal, they contended that "there was no consideration to support the issuance of the original issue shares" (Plaintiffs' Post-Trial Brief, p. 29); (Plaintiffs' Brief on Appeal p. 32).

In the prior action the exact same charge of issuing Transcontinental stock without consideration was alleged (A176):

> 22. From time to time, since on or about January 1, 1960 Fein had caused the stock of Trans to be issued at nominal, unfair and inadequate consideration to third parties whose names are not presently known to plaintiff, for the benefit of said defendant. Such issuance and sale of stock have been a waste of the assets of Trans....

The relief sought monetary damages against the defendants together with, among other things, a judgment (A178):

(e) Cancelling all shares of stock issued to the defendants or any of them or which, directly or indirectly, have unlawfully come into their ownership, possession or control since January 1, 1960.

Accordingly, Judge Conner's conclusion that plaintiffs' claim, attacking the issuance of the aforesaid 150,000 shares, was barred by the prior judgment is correct and should be affirmed.

The instant claim is identical to or at least "arising from, connected with or relating to" (A166) the matters alleged in the prior action; and certainly such claim "could have been asserted" (A166) in support of the allegations in the prior action.

Accordingly, the claim relating to the Original Issue Shares was properly dismissed as barred by the doctrine of res judicata.

E. All of the Claims Raised Under the First Count of the Complaint Are Barred by Limitations.

Since Judge Conner dismissed the first count on other grounds he did not deal with the issue of limitations. Had he done so he would have been compelled to dismiss all claims asserted by plaintiffs under this count as time-barred.

The complaint, filed in February of 1967, states in the first count, that Trenton and Fein "appropriated" 300,000 shares of Transcontinental stock, for which damages are sought (A12). At trial in 1974 plaintiffs sought to prove three distinct conversions of stock under the first count:

(a) The August 17, 1960 shares were claimed to have been wrongfully received by Fein and Trenton in 1960 (A98-99);

(b) The Collateral Security Shares were allegedly wrongfully purchased by Trenton in 1961 (A98);

(c) The Original Issue Shares were allegedly wrongfully turned over to Trenton under the letter of August 13, 1960 (A90).

Under the former Civil Practice Act an "action to recover damages for an injury to property" was subject to the three-year statute of limitations of C.P.A. § 49(7), which section was made specifically applicable to an action by "a corporation against a director, officer, or stockholder... to recover damages for waste or for an injury to property" by C.P.A. § 48(8). Thus, the alleged conversions of the August 17, 1960, shares and the Original Issue shares were time-barred before September 1, 1973, the effective date of the CPLR.*

The alleged conversion of the Collateral Security Shares was similarly time-barred in three years, or in 1964, because the CPLR continues a three-year limitation for "an action to recover... damages for the taking or detaining of a chattel," CPLR 214(3), or "to recover damages for an injury to property," CPLR 214(4). Klein v. Bower, 421 F.2d 338, 344 (2d Cir. 1970).

Apparently plaintiffs, while conceding that "the first and second counts clearly sound in conversion" (Plaintiffs' brief, p. 45), would have the court look to the six-year limitation of CPLR 213(7) on an action by a corporation against a

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* CPLR 218(a) provides that a cause of action barred under the Civil Practice Act on the effective date of the CPLR is to be unaffected by the new act.

director, officer, or stockholder. Even if this section were applicable, the only claim alleged in the complaint, relating to the August 17, 1960 shares, would have been time-barred before the commencement of this action in February 1967. The claims relating to the Collateral Security Shares and the Original Issue Shares would have long been barred when first raised at trial in 1974.

Plaintiffs' reliance on the tolling provisions of CPLR 203(f) is misplaced.* First, there was no comparable provision under the Civil Practice Act, which controls with regard to all but one of the alleged conversions.

Secondly, neither CPLR 214(3) and (4), which should control as to the Collateral Security Shares, nor CPLR 213(7), which plaintiffs apparently prefer, provides for computation of time from actual or imputed discovery. CPLR 203(f) is simply

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* Plaintiffs' partial quotation from CPLR 203(f) (Plaintiffs' brief, p. 47) misrepresents its meaning. The full quotation should have been (emphasis added):

> ...where the time within which an action must be commenced is computed from the time when facts were discovered or from the time when facts could with reasonable diligence have been discovered, or from either of such times, the action must be commenced within two years after such actual or imputed discovery or within the period otherwise provided, computed from the time the cause of action accrued, whichever is longer.

not applicable on any reading of this count.*

Finally, plaintiffs urge the applicability of the doctrine of equitable estoppel in an attempt to avoid the defense of limitations. The doctrine in New York is "sparingly enforced in exceptional instances" involving cases where a defendant's "deception and misrepresentation" caused plaintiff to delay in bringing suit. Augstein v. Levey, 156 N.Y.S. 2d 594, 598 (N.Y. Co. 1956). No deception, misrepresentation, or fraudulent concealment was ever proven by plaintiffs below.

None of the cases cited by plaintiffs in support of the doctrine of equitable estoppel is remotely comparable to this action except Standard Kollsman Industries, Inc. v. Sphere Brokerage Inc., N.Y.L.J., November 21, 1966, (N.Y. Co.), aff'd mem., 282 N.Y.S. 2d 921 (1st Dept. 1967), cited as involving "the precise issue involved in the instant litigation" (Plaintiffs' brief, p. 49). In that case, the court refused to apply the doctrine because of lack of proof of affirmative wrongdoing.

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* Friedman v. Myers, 482 F.2d 435 (2d Cir. 1973), inappropriately cited by plaintiffs (Plaintiffs' brief, p. 47) was a fraud case. The fraud statute of limitations, CPLR 213(8), does specifically provide for computation from the time of discovery. But this is not a fraud action. Saylor v. Lindsley, 302 F.Supp. 1174, 1180 (S.D.N.Y. 1969); Eisenberg v. Grossman, 84 N.Y.S.2d 118, 121-22 (Kings Cnty. 1948), app. dism. 87 N.Y.S. 2d 227 (2d Dept. 1949).

"Affirmative wrongdoing--a carefully concealed crime" on the defendant's part was found in General Stencils, Inc. v. Chiappa, 18 N.Y. 2d 125, 128, 272 N.Y.S.2d 337, 340 (1966). As the court said in Saylor v. Lindsley, 302 F.Supp. 1174, 1187 n.28 (S.D.N.Y. 1969), "New York's doctrine of equitable estoppel by way of fraudulent concealment is considerably less liberal than its federal counterpart in that an affirmative independent act of concealment on the part of the wrongdoer is required."

Erbe v. Lincoln Rochester Trust Co., 13 A.D.2d 211, 214 N.Y.S.2d 849 (4th Dept. 1961), app. dism., 11 N.Y.2d 754, 226 N.Y.S.2d 692 (1962), involved a trustee who concealed his self-dealing and the court decided merely that estoppel was a triable issue. The scarcity of similar New York decisions involving corporate officers* suggests that New York holds stockholders of corporations to a higher duty of vigilance than beneficiaries of trusts. See Note, "Developments in the Law:

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* Rank Organization Ltd. v. Pathe Laboratories, Inc., 33 Misc. 2d 748, 227 N.Y.S.2d 562 (N.Y. Co. 1962), also cited inappropriately by plaintiffs, did not turn on "duty to disclose" (Plaintiff's brief, p. 48), but rather involved gross attempts by the defendant to prevent the plaintiff from filing a timely objection.

Lowell Wiper Supply Co. v. Helen Shop, Inc., 235 F.Supp. 640 (S.D.N.Y. 1964), and Saylor v. Lindsley, supra, both decided only that the possibility of establishing estoppel precluded summary judgment on limitiations grounds, and both noted New York's strict construction of the doctrine.

Statutes of Limitations," 63 Harv. L. Rev. 1177, 1215 (1950). "Evidently, a stockholder, minority or otherwise, is supposed to keep himself informed so as to protect his interests." Augstein v. Levey, supra, 156 N.Y.S. 2d at 599.

Domination of a company by the alleged wrongdoers is not a sufficient reason for the application of the doctrine. As stated in Lowell Wiper Supply Co. v. Helen Shop, Inc., 235 F. Supp. 640, 645 (S.D.N.Y. 1964), "the period of limitation in a stockholders' derivative suit commences to run from the date of the perpetration of the wrong and not from the date of its discovery, notwithstanding continued domination by the allegedly recreant fiduciaries."

For all of the foregoing reasons, plaintiffs' claims under the first count (and the second count as well) are barred by the applicable statutes of limitations.

F. There Were No Infirmities in any Stock Certificates or Transfers

Plaintiffs contended for the first time at trial that many of the stock certificates which Trenton received, at various times, in connection with the transactions discussed above, should be voided because of improper facsimile signatures thereon. This specious issue was never previously pleaded and should not have been permitted to be raised. Nonetheless, the District Court rejected the argument out of hand at trial (Tr. 741-742).

All of the certificates received by Trenton and by Sackett and his group were properly signed in accordance with the by-laws of Transcontinental and the applicable Delaware statutes. The certificates bear the signature of a transfer agent, either

the Texas Bank, or defendant Fein, who involuntarily succeeded to the position when the Texas Bank refused to proceed until it was paid. In addition, the facsimile signature of an officer appears on all of the certificates. At trial Sackett argued that many of the certificates bore the signature of persons who were no longer officers of Transcontinental, a common practice of all companies which print up large amounts of stock certificates. Sackett chose to ignore the fact that the 650,000 shares he and his group acquired had the same alleged infirmities. The Court, however, duly noted the inconsistencies of plaintiffs' position when it commented that Sackett was willing to waive the infirmity of his own shares while seeking to declare everybody else's shares null and void (Tr. 741-742).

Plaintiffs contend that when facsimile signatures are used, the signature of the transfer agent must be some person other than the officer whose signature appears on the stock certificates as facsimilies. Neither a reading of Transcontinental's By-Laws or § 158 of the Delaware Corporation Law reveals any such requirement.

Transcontinental was insolvent from 1960 to at least 1966. It could not afford to pay a transfer agent. Fein, the company's only employee, and receiving no compensation for all of his efforts, with great reluctance, undertook the duties of the

transfer agent. He was thus both the transfer agent and sole employee of Transcontinental, not by choice but by reason of the financial difficulties of the company. Under the circumstances, plaintiffs' argument is preposterous.

In summary, and as already noted, all of the stock certificates which Transcontinental delivered to Trenton in exchange for previously outstanding certificates conformed with all of the requirements of Transcontinental's by-laws and Delaware law. This issue is one which the District Court rejected out of hand, which is devoid of merit and which plaintiffs should not be permitted to raise.

G. Conclusion

In summary, plaintiffs' claim for stock conversions under the first count of the complaint are barred by res judicata, collateral estoppel, release and limitations. Moreover, they are entirely devoid of merit.

Plaintiffs' claims that the stock transactions constituted a breach of fiduciary duty, a waste of the assets of Transcontinental, and self-dealing

were all the subject of the prior action and should be barred (A176-179). Moreover, the acts of defendant Fein in ousting Burkinshaw and in attempting to appease Trenton, a defrauded creditor were, in Judge Conner's words "eminently reasonable", "not the product of bad faith or even bad judgment" (A112).

For all of the reasons set forth above, the District Court's dismissal of the first count should be affirmed.

VI.

THE NINTH COUNT OF THE COMPLAINT WAS PROPERLY DISMISSED

TRENTON NEVER CONTRACTED TO SELL TO SACKETT ALL OF ITS SHARES OF TRANSCONTINENTAL AND NEVER REPRESENTED THAT 650,000 SHARES WERE ALL THE SHARES IT OWNED

In the ninth count of the complaint, plaintiff Sackett contended that on June 22, 1966 Trenton and Fein entered into a written agreement with him whereby "Trenton agreed to sell to Sackett all of the shares of TRANS owned by it", "wnich shares were represented by Trenton and Fein to aggregate 650,000 shares." (A20-22). Sackett claimed (a) that Trenton breached its contract to sell him "all" of its Transcontinental shares and (b) that Trenton falsely represented that it only owned 650,000 shares of Transcontinental stock.

The proof presented at trial demonstrated (1) that the June 22, 1966 agreement between the parties did not provide for the sale of "all" of Trenton's shares in Transcontinental, but was specifically limited to 650,000 shares and therefore there was no breach of contract and (2) that at no time did Trenton or Fein make any representation that Trenton only owned a total of 650,000 shares and therefore there was no misrepresentation.

After trial, the District Court concluded that plaintiffs "failed to carry their burden of establishing that the June 22, 1966 agreement provided for the sale of all of Trenton's Transcontinental stock, or that Trenton or Fein represented that Trenton owned only 650,000 shares of Transcontinental stock." (A131). Judge Conner's conclusions are amply supported by the evidence, are not clearly erroneous and should be affirmed.

A. The Terms of the June 22, 1966 Agreement are Unambiguous

The language of the contract is clear and unambiguous. It calls for the sale of specific assets to Sackett, which assets are clearly defined and listed. Among the assets sold to Sackett are 650,000 shares of Transcontinental stock. There is nothing vague or ambiguous about the description of the shares being sold. The contract contains no statement that Trenton agreed to sell "all" of its shares of Transcontinental. A specified number of shares is set forth. Moreover, nowhere does Trenton represent or imply that the 650,000 shares was all that Trenton held.

Paragraph Three of the June 22, 1966 agreement lists numerous warranties and representations made by Trenton and Fein. There is no warranty or representation that the 650,000 shares constituted "all" of Trenton's holdings.

The contract between the parties is thus neither vague nor ambiguous. On the contrary, it is quite specific. The parole testimony offered by plaintiffs in an attempt to vary the terms of this very specific agreement should not have been permitted. It is irrelevant as to what Mr. Sackett believed the June 22, 1966 agreement meant. The clear language must control.

Both sides to the contract were represented by counsel. Irwin Taylor, counsel for plaintiffs, represented plaintiff Sackett. Lewis G. Cole, a member of the firm of Stroock & Stroock & Lavan, represented Trenton and Fein. Mr. Cole testified that Mr. Taylor never asked for the inclusion of a warranty or representation that 650,000 shares were all of the shares owned by Trenton (Tr. 1287).

Moreover, Mr. Cole, an attorney with many years of experience in handling corporate acquisitions and sales and purchases of shares, gave the following unrebutted testimony:

> If the object of the transaction is to acquire all of the shares owned by a person, it would be customary to have that person represent and warrant that the shares in question were his total holdings. (Tr. 1292).

No such warranty was requested and none was given. The obvious reason for that is that Trenton had agreed to sell 650,000 shares and not all of its shares. That is the number of shares delivered to Sackett and, therefore, there was no breach of contract.

B. There Were No Oral Misrepresentations

On deposition, Sackett claimed that he had entered into an "oral agreement" with defendants to acquire all of Trenton's shares (A261-263). However, in view of the clear bar of the parole evidence rule, plaintiffs abandoned their reliance upon an alleged "oral agreement, and urged instead that defendants made fraudulent misrepresentations. However, plaintiffs presented no proof that defendants Trenton and Fein ever represented to Sackett that the 650,000 shares of Transcontinental were "all" of the shares owned by Trenton.

Sackett admitted on his deposition that Fein never represented to him that Trenton only owned 650,000 shares (A560):

> Q I am asking you a question that I believe can be answered yes or no. I want to know whether Mr. Fein ever told you that Trenton Products only owned 650,000 shares of Transcontinental? Either he said that to you on some occasion, or he never said it to you.

A At any time?

Q At any time, did he ever tell you that Trenton Products only owned 650,000 shares?

A I don't think he ever told me that at any time, as to what specifically Trenton owned."

At trial, Sackett, on direct examination, changed his testimony and for the first time recalled (Tr. 223):

> When I asked Mr. Fein whether the 650,000 shares was all the shares that Trenton had that was part of this deal, he replied, 'Yes, but I have some stocks in my own name...'.

When confronted with his deposition testimony on cross-examination he again changed his testimony and admitted that Fein did not tell him that 650,000 shares was all of the shares in Transcontinental that Trenton owned (Tr. 234):

Q Now I ask you: Did Mr. Fein tell you that 650,000 shares was all the shares in Transcontinental that Trenton owned? Yes or no.

A Directly, no.

The above was the only proof presented by plaintiffs on the alleged oral representation. It demonstrates that plaintiffs' claim of an alleged oral representation was properly disbelieved by Judge Conner. No oral representations were made by defendants and none were proven.

As noted above, the question of whether or not Sackett believed he was contracting for "all" of Trenton's shares, or whether or not Fein believed that Trenton was contracting to sell 650,000 shares is irrelevant. The contract is clear and unambiguous and speaks for itself. There was no need to inquire into the subjective intent of the parties. Nevertheless, since the District Court permitted this line of testimony, the testimony demonstrated that Sackett knew or could have known and

didn't care, that the defendants Trenton and Fein would continue to own shares of Transcontinental after Sackett's purchase of the 650,000 shares.

At the first meeting when the parties explored the possibility of settling the derivative litigation, Sackett testified that the parties discussed Fein's "getting out of Transcontinental completely and selling his and Trenton's interests to me" (Tr. 50, 53) for a figure or some $280,000 (Tr. 239-240). Fein confirmed Sackett's recollection and testified that during the initial discussions he wanted some $285,000 (Tr. 627). During the course of the negotiations, Sackett advised Fein that he had difficulties raising the necessary funds and the parties discussed the possibility of Sackett's paying less than $280,000 and receiving less than all of the shares owned by Trenton and Fein. Varying amounts of stock were discussed, ranging from 350,000 to 650,000 shares (Tr. 627-628). The parties finally agreed that Sackett would pay $187,500 to Trenton for the loan obligation owed to Trenton by Transcontinental and that Trenton would deliver to Sackett and his group 650,000 of the shares of Transcontinental stock which it owned (Tr. 240). Of the shares owned by Fein, none were included in the sale.

In accordance with the above, and on June 22, 1966, the written contract was entered into between Trenton and Sackett.

Sackett and his group, through the acquisition of the 650,000 shares, together with another 286,510 shares owned by them prior to August 12, 1966, took over the management and

control of Transcontinental (Defendants' Exhibit EEE, FFF, CCCC, XXXX, AAAAA and GGGGG). It was thus not necessary for Sackett to acquire all of the shares owned by Fein and Trenton in order to obtain control of Transcontinental. Indeed, that is precisely why the contract contains no representation that these were "all" of the shares owned by Trenton. That fact was not important to Sackett since his group owned and was acquiring a total of 936,510 shares, more than sufficient to control Transcontinental.

Finally, Exhibit VVVV is a draft stipulation of settlement prepared by Sackett's own counsel in connection with the settlement of the 1965 litigation. Paragraph I thereof specifically lists among the assets to be sold by Trenton to Sackett's group: "650,000 shares of the common stock of Trans now held by Trenton of record or beneficially." The foregoing demonstrates that Sackett well knew that he was only to acquire 650,000 shares "of the common stock of Trans now held by Trenton."

Plaintiffs' argument that an affidavit submitted by their counsel on the settlement of the 1965 derivative action demonstrates Sackett's belief at the time that he was to get all of Trenton's shares was correctly rejected by Judge Conner. That affidavit refers to the sale of specific assets, including the 650,000 shares. Nowhere does it state or imply that the 650,000 shares was all that Trenton held. Similarly misplaced was plaintiffs' reliance below upon a blanket Trenton corporate resolution giving discretion to and authorizing Fein to sell securities owned by Trenton, including shares of Transcontinental. This is a simple resolution authorizing an officer to sell any,

and up to all, of the securities owned by a company. It in no way proves that Sackett and the defendants had agreed to the sale by Trenton of all of its Transcontinental stock. Judge Conner properly rejected plaintiffs' contention and, on the basis of all the evidence, properly concluded that Trenton did not contract to sell all of its shares and never falsely represented that 650,000 shares were all of the shares it owned. Accordingly, the ninth count of the complaint was properly dismissed.

VII.

THE TENTH COUNT OF THE COMPLAINT WAS PROPERLY DISMISSED

DEFENDANTS DID NOT BREACH THEIR WARRANTY UNDER THE JUNE 22, 1966 AGREEMENT

Sackett brought this count for alleged breach of warranty under the June 22, 1966 agreement. Sackett contends that defendants warranted that there were 3,600,000 shares of Transcontinental outstanding when in fact there were 3,977,605 shares of Transcontinental outstanding.

Judge Conner correctly dismissed this claim of breach of warranty.

The June 22, 1966 agreement specifically provides:

> THIRD: Trenton and Fein hereby warrant and represent to Buyer [Sackett] that to the best of Fein's actual knowledge and the actual knowledge of Trenton, as obtained through Fein who is its President:
>
> * * *
>
> (h) The issued and outstanding stock of Transcontinental consists of not more than 3,600,000 shares of common stock.

Judge Conner properly concluded that Sackett was "unable to prove that Fein personally, or Trenton through Fein, had actual knowledge that the number of issued and outstanding shares of Trans common stock was greater than the maximum of 3,600,000 shares he warranted." (A137). In so holding, the District Court took note of the fact that the "stock records of the company had been in hopeless confusion since Texas Bank & Trust Co. had ceased to act as transfer agent and had retained the records as security for the money owed it." (A137). All

parties were fully aware of the company's insolvency and the disorganized state of affairs of its records. Moreover, the company's records had been moved to Canada by Burkinshaw in 1960, creating further confusion as to the precise number of shares of the company which might be outstanding.

The parties knew of the company's disorganized condition. That is precisely why they agreed to narrowly limit, in the June 22, 1966 agreement, Trenton's liability for any breaches (A370).

In making the warranty, Trenton used the most recent annual report filed with the Delaware Secretary of State which reflected a total of 3,600,000 shares outstanding (Tr. 746). Trenton and Fein believed that figure to be accurate.

The District Court, considering the entire record relating to Transcontinental's disorganized state of affairs due to its insolvency, correctly concluded that Sackett failed to prove that Trenton had "actual knowledge" that more than 3,600,000 shares were outstanding. Sackett's claim for breach of warranty was thus properly dismissed.

VIII.

ALTERNATIVELY, THE NINTH AND TENTH COUNTS SHOULD HAVE BEEN DISMISSED ON THE GROUNDS OF LACK OF DIVERSITY JURISDICTION

In the event this Court reverses the dismissal on the merits of the ninth and tenth counts, those counts should be dismissed for lack of diversity jurisdiction.

A. Collusive Jurisdiction

The proof at trial established that Sackett and those upon whose behalf he allegedly sued had improperly and collusively sought to invoke the jurisdiction of the District Court.

28 U.S.C. 1359 specifically condemns efforts to collusively establish diversity jurisdiction:

> A district court shall not have jurisdiction of a civil action in which any party, by assignment or otherwise, has been improperly or collusively made or joined to invoke the jurisdiction of such court.

By agreement dated June 30, 1966, a syndicate of eleven investors, including Sackett, entered into an agreement governing their relationship with respect to their common investment in Transcontinental (Exhibit HHHH). Paragraph III of said agreement provides in relevant part as follows:

> III. A. The Trans Investment shall be held in the names of Phillip P. Goodkin, Judson L. Streicher and Harry B. Leslie, jointly as nominees (hereinafter "Agents"), for the benefit of and as Agents for the investors.
>
> ....
>
> C. The exercise of any of the rights and privileges incident to said Trans Investment, including but not limited to the enforcement of the rights of declaration of default, foreclosure, conversion, voting or the institution of litigation, on behalf of the investors by the said Agents shall be effective only if authority therefor shall be given in writing by a majority of the undersigned investors.

D. For the purpose of this Paragraph, a majority of the undersigned investors shall be deemed to be investors then owning more than fifty (50%) percent of the Trans Investment Units."

Messrs. Goodkin, Streicher and Leslie, the "Agents" for the group for purpose of "the institution of litigation," are all citizens of New York, as is defendant Fein (A385). Mr. Sackett is a resident of Connecticut (A385). Thus, the ninth and tenth counts of the complaint, for breach of contract and misrepresentation in connection with the June 22, 1966 agreement could not have been brought in the Federal Courts by Messrs. Goodkin, Streicher and Leslie. Accordingly, in an effort to create the facade of diversity jurisdiction the action was instituted, not by one or all of the "Agents" of the group, but by Sackett, a Connecticut resident, in direct violation of 28 U.S.C. § 1359.

Of the $320,000 invested by the eleven members of the syndicate, Sackett's contribution amounted to only 3/48 of the entire investment (A385 and Exhibit HHHH, pages 9-10). His interest is minor in relation to the financial interest of the parties he claimed to represent. Nevertheless, although he clearly does not have the dominant financial control over the investment he is the only individual plaintiff. It is quite obvious that he chose this device in order to attempt to improperly impose jurisdiction upon the District Court. The extent to which he sought to cover up this charade was apparent at trial when he strenuously resisted the production of the syndicate agreement.

Whenever persons retain a substantial pecuniary interest in and power over the outcome of litigation, the action is collusive if brought by another. J.F. Pritchard & Co. v. Dow Chemical of Canada Ltd., 331 F.Supp. 1215 (D.C. Mo. 1971), affd., 462 F.2d 998 (8th Cir. 1972); Steinberg v. Torro, 95 F.Supp. 791 (D.P.R. 1951). The federal courts should not condone such attempts, as exist here, at manufactured diversity jurisdiction.

B. The Citizenship of The Syndicate Members Controls

Had Sackett desired, he could have sued in the federal court for his interest and his own damages in his individual capacity. However, he saw fit to not only sue for his individual damages but for damages for others, claiming he was their nominee. He has standing to do so under Federal Rule 17(a)*. However, since those persons on whose behalf he purports to act are citizens of New York, diversity jurisdiction is defeated.

As stated by Judge Timbers in Stonybrook Tenants Assn. v. Alpert, 194 F.Supp. 552, 556 (D. Conn. 1961):

> For purposes of determining whether requisite diversity of citizenship exists, the courts look to the citizenship of the real parties in interest and disregard the citizenship of nominal or formal parties having no real interest in the controversy.

In the case at bar plaintiff Sackett characterizes himself as "nominee" and makes it clear that he is, as to those he claims to be acting for, a mere nominal party without equitable or beneficial ownership of the claim. In a suit in which it

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* Standing to sue on the part of a plaintiff should not be confused with jurisdiction to entertain his suit by the court. A plaintiff may well have standing to sue but it must be in a court which has jurisdiction over his claim.

appears by the record that a party has no interest, such a plaintiff has been held to be a nominal party whose citizenship is disregarded for the purpose of the diversity statute. Stonybrook Tenants Assn. v. Alpert, 194 F. Supp. 552 (D. Conn. 1961); see 3A Moore, Federal Practice (2d ed. 1974) ¶ 17.04.

We are cognizant of the cases that hold where a party sues as a receiver, representative of a class, assignee, subrogee, executor or administrator, it is normally his citizenship that is material when jurisdiction is dependent on the character of the parties. However, those cases have no application to the case at bar. First, 28 U.S.C. 1359 precludes Sackett's representative status since it was invoked to create diversity. Secondly, as pointed out in 3A Moore, Federal Practice (2d ed. 1974) ¶ 17.04, at 114, if the substantive law of the state gives the administrator, guardian or representative the status of only a nominal fiduciary, the beneficiary or ward, not the administrator or guardian, is the real party in interest and it is the citizenship of the beneficiary or ward, as the case may be, that is determinative of diversity jurisdiction.

Thus, the question is resolved by an analysis of whether the plaintiff is a nominee or has a real interest. In the case at bar the plaintiff concedes, in entitling the action, that he is a mere nominal party as to those he claims to represent.

For the reasons set forth above, if the District Court's dismissal of the ninth and tenth counts on the merits is reversed, this Court should dismiss those counts for lack of jurisdiction.

CONCLUSION

In this litigation plaintiffs have sought to make defendants account for transactions which occurred approximately 14 years prior to trial and with respect to a company which, in plaintiffs' counsel's own words, was "moribund" and "on the verge of insolvency". The company's records, over the years, were in many hands, in Canada and back in this country, and out of defendants' possession since 1966. In pre-trial discovery, defendants fully responded to the claims set forth in the complaint At trial, plaintiffs shifted position and sought to attack entirely different transactions, continuously asking defendants to respond to new and baseless charges. Defendants have demonstrated the lack of merit of all of plaintiffs' claims. Furthermore, under the circumstances of this case, and in the interests of justice, the defenses of res judicata, collateral estoppel, release, and limitations should be strictly applied. Accordingly,

(a) The judgment entered on the second count in the amount of $48,200, with interest from 1966, should be reversed and the second count should be dismissed;

(b) The judgment dismissing the first, second and third counterclaims should be reversed and remanded to the District Court for a trial on the issue of damages, and

(c) The judgment dismissing the first, ninth and tenth counts should be affirmed.

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Service of three (3) copies of the within
is hereby admitted this 9 day of
Feb 1977.

Kaufman Taylor Kimmel & Miller
Attorneys for Plaintiffs-Appellees